CLEVELAND PUBLIC LIBRARY
BUSINESS INF. BUR.
CORPORATION FILE

58

NATIONAL TEA CO.

Annual Report to Shareholders

National Tea Co., home office: 1000 N. Crosby St., Chicago 10, Ill.

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TRANSFER AGENTS

The First National Bank of Chicago
Chicago, Illinois

The Chase Manhattan Bank
New York, New York

REGISTRARS

Continental Illinois National Bank & Trust Company of Chicago
Chicago, Illinois

The New York Trust Company
New York, New York

TRUSTEES AND PAYING AGENTS

3½% Debentures
Chemical Corn Exchange Bank
New York, New York

5% Debentures
J. P. Morgan & Co.
New York, New York

DIRECTORS

NORBERT L. CHAPLICKI
Vice President

JOHN F. CUNEO*
President of The Cuneo Press, Inc.

D. LLOYD McCLOCKLIN
Assistant Secretary of Loblaw Groceterias, Ltd.

HARLEY V. McNAMARA*
President and Chief Executive Officer

ROY S. McPHERSON
Partner, Thorne, Mulholland, Hawson & McPherson (chartered accountants)

RICHARD G. MEECH
Vice President, Secretary and Treasurer of Loblaw Groceterias Co., Ltd.

GEORGE C. METCALF*
Chairman of the Company and President of Loblaw Groceterias Co., Ltd.

CLAUDE H. WEBSTER
Executive Vice President

W. GARFIELD WESTON
Chairman of the Board of George Weston, Ltd.

**Members of the Executive Committee*

OFFICERS

GEORGE C. METCALF
Chairman of the Company

HARLEY V. McNAMARA
President and Chief Executive Officer

CLAUDE H. WEBSTER
Executive Vice President

NORBERT L. CHAPLICKI
Vice President

VAL S. BAUMAN
Vice President

IRA O. SHY
Vice President

GEORGE E. HOUSTON
Vice President

HAROLD L. WILKENS
Vice President

E. GUY LOY
Vice President

NORMAN A. STEPLETON
Vice President

CHARLES WOODING
Treasurer

ROBERT E. KOEHLER
Comptroller and Asst. Treasurer

WILLIAM T. MORGAN, JR.
Secretary

COVER ILLUSTRATION • ROSELAND SHOPPING CENTER • CHICAGO, ILLINOIS
INTERIOR PHOTOGRAPHS • GLENDALE SHOPPING CENTER • INDIANAPOLIS, INDIANA

National Branch Offices and Warehouses • Chicago • Minneapolis • Milwaukee • Indianapolis • Detroit • Kalamazoo • St. Louis • New Orleans • Memphis • Davenport • Denver • Sioux City

National Food Stores Serving The States of • Alabama • Arkansas • Colorado • Illinois • Indiana • Iowa • Louisiana • Michigan • Minnesota • Mississippi • Missouri • Nebraska • North Dakota • Ohio • South Dakota • Tennessee • Wisconsin • Wyoming

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NATIONAL FOOD STORES

Financial Highlights

	1958 (53 weeks)	1957 (52 weeks)
OPERATIONS:		
Sales	$794,162,135	$681,131,958
Profit before income taxes	17,741,543	16,773,752
Federal income taxes	8,900,000	8,720,000
Net profit	8,841,543	8,053,752
Net Profit—Percent to sales	1.11%	1.18%
Cash dividends	4,371,576	4,292,508
Earnings retained in the business	4,469,967	3,761,244
INVESTMENT:		
Working capital	46,446,339	51,038,713
Plant and equipment	62,597,533	53,834,125
Long-term debt	39,485,000	42,539,220
Common shareholders' equity	68,858,804	61,800,977
PER COMMON SHARE:		
Profit (based on average shares outstanding)	4.03	3.76
Dividends	2.00	2.00
Equity	31.00	28.52
Shares outstanding	2,221,418	2,167,068
TOTAL STORES		
—at end of year:	932	883

58 Management Report to the Shareholders of National Tea Co.

H. V. McNamara
President

Management Report for 1958

"Progress despite problems" is the record for 1958. We are proud of our continued progress in 1958 to record highs in sales and profits, but we are also aware of the problem of declining profit margins, which now is facing the entire industry. The rapid growth of supermarkets has created increased competition for customers, and as a result, some operators have either forgotten or ignored sound business ethics and economics. Selling below cost, for example, like hitting below the belt, is, in our opinion, an unsound and unfair method of competition, which destroys profits, and in the long run can adversely affect the service to the consumer.

Our policy at National is to combat competition, no matter how unfair, to protect our position in the market. We are hopeful, that after the industry has an opportunity to analyze its earnings for 1958, and finds that in many instances the sales increases for the year did not produce corresponding increases in profits, operators might merchandise with a little more intelligence in 1959. This is essential to the improvement of earnings, and the continued steady growth of the industry. In our opinion a profit margin of 1.5 per cent of sales would be fair to everybody, operators, shareholders, and consumers alike.

Sales

Total sales of $794,162,135 for the 53 weeks ended January 3, 1959 were 16.6 per cent greater than last year's record $681,131,958, achieved in 52 weeks. The $113,030,177 increase in sales for 1958 is the greatest advance experienced in one year over the entire history of the company. Sales per store in 1958 averaged $16,500 per store per week, as compared with $15,900 per week in 1957, and only $8,000 per week ten years ago.

This report, in respect for brevity, reviews our progress for only ten of the past fourteen years under present management. However, for the record, it can be said that our sales for 1958 were 700 per cent ahead of 1944, the last year under former management, and our number of stores has been increased only 12 per cent in this time, although, of course, our present stores are greatly improved in size, quality and location.

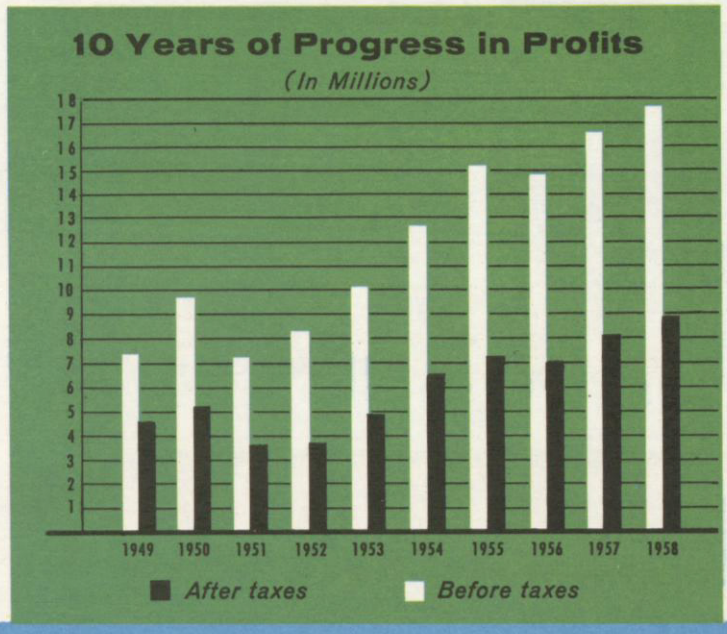
Profits

Net profit of $8,841,543 for 1958 was $787,791 greater than 1957, for a gain of 9.78 per cent over last year's record $8,053,752. Based on average shares outstanding during the year, this is equivalent to $4.03 per common share, or 27 cents more per share than last year.

This increase of almost 10 per cent in earnings did not keep pace with sales for several important reasons: To begin with, we had to fight recession, particularly in the industrial areas of Michigan, Ohio, Indiana and parts of Illinois, where wage earners depend on the durable goods manufacturers for their weekly income. Sales were maintained at fairly satisfactory levels, considering the affect on the individual marketing areas, but at a cost in the form of reduced rate of profit. The strike in Minneapolis, reported to shareholders on December 1, 1958, completely closed down one of our largest branches for a period of almost two weeks, with loss of sales and even more reflection on profits. Intensified competition in several trading areas forced us to sacrifice profit margins in order to maintain traffic and hold customers to our stores.

For these reasons, as well as the increased cost of doing business, which showed no tendency to reverse itself during the recession

President's Letter Continued on Page 3



1958

Distribution of National's Sales Dollar

	1958
Merchandise	.8094
Employees	.1062
Taxes	.0167
Rent, depreciation and repairs	.0286
Other expenses	.0280
Dividends paid to shareholders	.0055
Profit retained in the business	.0056
	1.0000

period, our increase in earnings did not keep pace with the increase in sales.

Dividends and Shareholders' Equity

Cash dividends were maintained in 1958 at the rate of 50 cents per quarter existing since 1956. Total payments for the year were $2.00 per share. About one-half the profit for 1958 was retained in the business, and has been used to finance the expansion program. Shareholders' equity is now $31.00 per share, an increase of $2.48 for the year.

The return on the shareholders' equity has been maintained at about 13.5 per cent of the average balance for both 1958 and 1957, so we feel that your funds are being soundly re-invested for greater profits.

Operations

After 1957's extraordinary expansion into 3 new states and many large trading areas, 1958 can best be described as a consolidation of previous gains. No new states, and only one large trading area, Peoria, Illinois, were entered in 1958. However, 95 new stores were opened in 1958, a new record of internal expansion in a single year, and an additional 28 stores were acquired from regional operators within our territory. During 1958 we closed a total of 74 stores, which were obsolete and too small to continue operating profitably. Some of these stores in desirable trading areas were replaced with new larger stores, and some were those which we had taken over in our Sioux City branch and other recent acquisitions, which had to be weeded out, because they offered no promise for continued operation. This resulted in a net increase of 49 in number of stores operated as of January 3, 1959, bringing our total to 932 retail stores operating in 18 states.

A favorable option to purchase from the lessor the warehouse and office building of our Denver branch was exercised in January, 1958. We now own the warehouse and office buildings occupied by 3 of our 12 branch distribution centers.

Financial

In line with a majority of the industry, we have reclassified prepaid expenses and current deferred charges, comprising items which will be amortized in 12 months or less, as current assets. This amount has been added to working capital, which at January 3, 1959, aggregated $46,446,339, down $4,592,374 from 1957 as indicated in the following summary.

Source of Funds:	
Net Income	$ 8,841,543
Deferred Federal Income Taxes (related to accelerated depreciation)	810,000
Sale of 10,980 common shares to optionees	390,382
Treasury common shares used for acquisitions	305,866
	$10,347,791
Disposition of Funds:	
Net expenditures for plant and equipment in excess of depreciation and amortization	$ 4,175,078
Acquisitions of other businesses	4,487,441
Retirement of long-term debt	1,155,023
Cash dividends on common shares	4,371,576
Other dispositions, net	751,047
	$14,940,165
Decrease in working capital	$ 4,592,374

President's Letter Continued on Page 4

President's Letter Continued from Page 3

Working capital requirements for normal business operations have been satisfactorily met from retained earnings and depreciation provisions, and projections for 1959 indicate no change in this picture. Future requirements for additional financing, if any, will depend solely on whether future acquisitions of food chains will be for cash or stock. While we are continuously exploring opportunities for expansion through such acquisitions, Federal income tax regulations tend to discourage cash transactions in favor of stock exchanges.

The Company self-insures certain casualty risks, where the exposure is wide-spread. In 1958, a so-called "umbrella" insurance policy was purchased under which the company is protected on losses in excess of $500,000. Accordingly, the self-insurance reserve was reduced after providing for all claims at January 3, 1959, to a balance of $500,000 less Federal income taxes thereon or a net amount of $250,000.

Organization and Personnel

Four new vice presidents were named in 1958 to further define the company's plan of organization and to provide greater depth for the management team. All of these new officers, like their associates, have many years of sound experience in the food business.

Many other promotions of qualified personnel to positions of leadership and responsibility were made during the year as the rapid growth of the business continues to create opportunities for advancement open to all of our more than 15,000 full time and 7,000 part-time employees who desire to get ahead. There is no greater thrill than observing the progress of eager young men and women, who are realizing the fruits of their ambition and hard work as they climb up the ladder of success. Our heartfelt thanks and appreciation go out to every one of these our co-workers, without whom this report of progress could not be written.

Additional employee stock options have been granted under the plan approved by shareholders on March 21, 1957. Options to purchase 50,000 shares of common stock, as authorized, have been granted to 121 officers and key employees in amounts ranging from 200 to 1,000 shares each. Stock purchases under the plan are giving these key employees a deeper interest in the company.

Outlook for 1959

The food industry set the pattern for business leadership in 1958, a year which started with gloomy predictions of recession, and ended with high notes of optimism. We feel that this momentum will carry into 1959, and that the renewed consumers' confidence in the economy will maintain spending at a satisfactory level. It looks like another year of record sales and profits at National.

H. V. McNamara
President

Chicago, Illinois
February 25, 1959

10 Year Review of Financial Highlights

Continued Progress Report 1949—1958

Following Reported in Thousands (000 Omitted)

YEAR	1958 53 WEEKS	1957	1956	1955	1954	1953	1952	1951	1950	1949
OPERATIONS:										
Sales	$794,162	$681,132	$617,636	$575,585	$520,300	$462,282	$405,220	$361,321	$315,219	$274,332
Profit Before Federal Taxes	17,742	16,774	14,938	15,237	12,739	10,048	8,408	7,203	9,765	7,420
Federal Taxes	8,900	8,720	7,930	8,000	6,220	5,150	4,690	3,595	4,550	2,848
Net Profit	8,842	8,054	7,008	7,237	6,519	4,898	3,718	3,608	5,215	4,572
Percent to Sales	1.11%	1.18%	1.13%	1.26%	1.25%	1.06%	.92%	1.00%	1.65%	1.66%
Cash Dividends:										
Preference	—	—	—	1	212	450	504	266	107	125
Common	4,372	4,293	4,241	4,198	2,961	2,594	2,498	2,466	2,001	2,000
Earnings Retained Before Special Items	4,470	3,761	2,767	3,038	3,346	1,854	716	876	3,107	2,447
INVESTMENT:										
Working capital	46,446①	51,039①	42,633	44,112	34,118	30,002	22,586	24,002	16,567	16,181
Plant and equipment	62,598	53,834	43,143	38,530	29,499	25,457	19,413	17,293	15,118	12,533
Long-term debt	39,485	42,539	30,103	30,700	16,200	16,200	4,200	4,600	5,000	5,100
Common shareholders' equity	68,859	61,801	56,286	53,499	45,929	35,538	30,239	28,913	28,285	24,768
Shares outstanding	2,221	2,167	2,121	2,120	1,971	1,707	1,568	1,542	1,541	769
									Following Reported in Actual Amounts	
PER COMMON SHARE:										
Profit	4.03④	3.76④	3.30	3.41	3.20	2.65	2.05	2.14	3.31	2.89③
Dividends	2.00	2.00	2.00	2.00	1.60③	1.60	1.60	1.60	1.60	1.25②
Equity	31.00	28.52	26.54	25.23	23.30	20.81	19.28	18.75	18.40	16.09②
TOTAL STORES										
At year end	932	883	761	744	711	688	765	624	634	655

① Prepaid expenses included in working capital since 1957.
② 1949 per share amounts adjusted for two for one split on December 20, 1950.
③ Plus extra 2% stock dividend paid to shareholders of record on November 16, 1954.
④ Profit per share since 1957 computed on average shares outstanding.

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Consolidated Balance Sheet

National Tea Co. and Subsidiaries

ASSETS

CURRENT ASSETS:

Cash

U. S. Government securities

Accounts receivable

Inventories, at lower of cost or market—
Merchandise

Supplies

Prepaid expenses

Total current assets

OTHER ASSETS

PLANT AND EQUIPMENT, at cost, less reserves for depreciation

Land

Buildings

Fixtures and equipment

Reserves for depreciation

Leasehold improvements, less amortization

Excess of cost of investment in branches and subsidiaries over underlying book values at dates of acquisition—in process of amortization

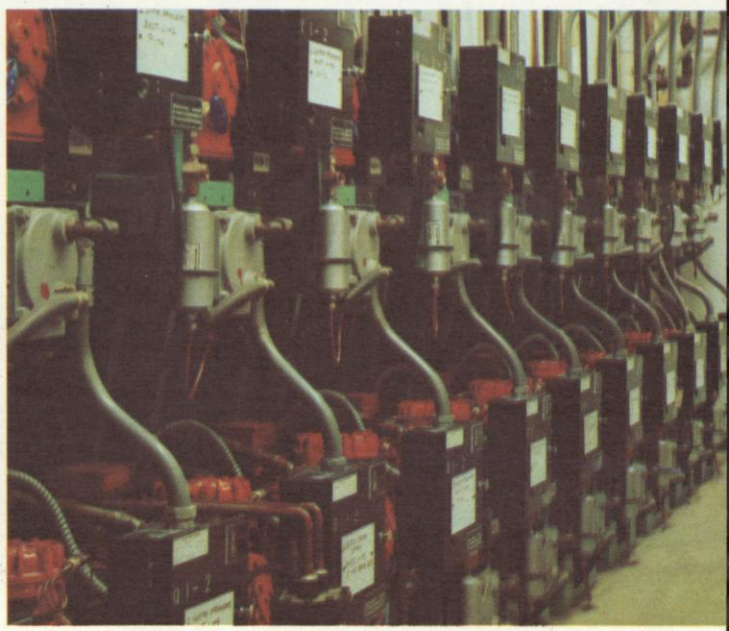
NATIONAL FOOD STORES

Jan. 3, 1959	Dec. 28, 1957
$ 19,372,767	$ 23,522,036
——	499,158
4,218,316	4,930,797
54,824,715	51,176,788
1,611,476	1,604,532
3,261,674	2,539,728
$ 83,288,948	$ 84,273,039
$ 2,091,860	$ 1,793,094
$ 1,964,113	$ 1,804,854
9,951,711	8,072,775
66,073,735	59,074,236
(30,237,795)	(26,977,374)
13,181,507	10,051,511
$ 60,933,271	$ 52,026,002
1,664,262	1,808,123
$ 62,597,533	$ 53,834,125
$147,978,341	$139,900,258

LIABILITIES

	Jan. 3, 1959	Dec. 28, 1957
CURRENT LIABILITIES:		
Current maturity of long-term debt (including $75,000 debt of subsidiary)	$ 1,155,000	$ 550,000
Accounts payable	24,766,404	22,074,471
Accrued liabilities	4,864,726	4,612,610
Federal income taxes	6,056,479	5,997,245
Total current liabilities	$ 36,842,609	$ 33,234,326
LONG-TERM DEBT:		
3½% sinking fund notes of subsidiary, due 1971	$ 861,000	$ 936,023
4% promissory notes, due 1973	14,100,000	14,700,000
5% sinking fund debentures, due 1977	11,520,000	12,000,000
3½% sinking fund subordinated debentures, due 1980 (convertible into common shares through 1965)	13,004,000	14,903,197
	$ 39,485,000	$ 42,539,220
RESERVES:		
Deferred Federal income taxes (relating to accelerated depreciation)	$ 2,530,000	$ 1,720,000
Self-insurance	250,000	581,951
Minority interest in consolidated subsidiary	11,928	23,784
	$ 2,791,928	$ 2,325,735
CAPITAL STOCK AND SURPLUS:		
Preference shares—authorized 30,000 shares	$ ——	$ ——
Common shares, par value $5— Authorized, 4,300,000 shares Issued: 1958—2,225,298 shares; 1957—2,181,630 shares	11,126,490	10,908,150
Reserved for options and conversions—290,641 shares		
Paid-in surplus	19,557,760	17,601,835
Earned surplus	38,352,218	33,882,251
	$ 69,036,468	$ 62,392,236
Less—Cost of treasury common shares— 1958—3,880 shares; 1957—14,562 shares	177,664	591,259
	$ 68,858,804	$ 61,800,977
	$147,978,341	$139,900,258

See notes to financial statements.



Statements of Consolidated Income and Surplus

NATIONAL TEA CO. and SUBSIDIARIES

INCOME	1958 53 weeks	1957 52 weeks
SALES	$794,162,135	$681,131,958
COSTS AND EXPENSES:		
Cost of sales and expenses	$755,088,835	$646,818,309
Depreciation and amortization	7,759,208	6,697,392
Rent	11,672,077	9,415,827
Interest	1,900,472	1,426,678
Federal income taxes	8,900,000	8,720,000
	$785,320,592	$673,078,206
NET INCOME	$ 8,841,543	$ 8,053,752

EARNED SURPLUS

BALANCE AT DECEMBER 28, 1957	$33,882,251
NET INCOME FOR 53 WEEKS	8,841,543
	$42,723,794
DEDUCT—Dividends paid on common shares ($2.00 per share)	4,371,576
BALANCE AT JANUARY 3, 1959	$38,352,218

PAID-IN SURPLUS

BALANCE AT DECEMBER 28, 1957		$17,601,835
ADD OR (DEDUCT)		
Excess of market value over cost of treasury common shares issued in exchange for assets and stock of new businesses acquired	17,272	
Excess of cost over option price of 5100 treasury common shares sold to officers and employees	(41,739)	
Excess of proceeds over par value of 5880 new common shares sold to officers and employees under stock option plan approved by shareholders on March 21, 1957	180,917	
Excess of principal amount of debentures retired over par value of 37,788 common shares issued in conversion	1,799,475	
BALANCE AT JANUARY 3, 1959		$19,557,760

See notes to financial statements.

Notes to Financial Statements

Long-term Debt

The 4% promissory notes require annual prepayments of $600,000 in 1959 through 1961, $700,000 in 1962 through 1964 and $1,000,000 in 1965 through 1972.

The 5% sinking fund debentures require mandatory sinking fund payments sufficient to retire $480,000 debentures in each of the years 1959 through 1972 and $600,000 of debentures in each of the years 1973 through 1976. Additional optional sinking fund payments may be made each year sufficient to retire at the same price debentures not in excess of 50% of the mandatory retirements.

The 3½% subordinated debentures require annual sinking fund payments of $350,000 in 1959 through 1969, $360,000 in 1970 through 1974 and $370,000 in 1975 through 1979. The debentures are convertible into common shares at $52.75 through November 1, 1959, $55.25 through 1962 and $57.75 per share through 1965.

Dividend Restriction

Earned surplus of $24,546,260 is restricted as to the payment of cash dividends on and the purchase of common shares at January 3, 1959; net current assets remaining after giving effect to the payment of dividends or reacquisition of stock must equal at least $25,000,000.

Litigation

In 1956 a suit was filed against the company and certain of its officers and directors by two alleged stockholders attacking (1) the sales by Messrs. Cuneo and Rasmussen to Loblaw Groceterias, Co., Limited, in January, 1956, of all, or substantially all, their stock holdings and (2) purchases made by the company from certain companies in which Mr. Cuneo is financially interested. No liability is asserted against the company.

The suit filed against the company in 1952 by certain alleged stockholders (described in previous reports) was dismissed in 1958 at the request of the plaintiff.

Stock Options

As of January 3, 1959, option agreements are outstanding with officers and employees granting them the right prior to October 26, 1959, to purchase 1000 common shares at $33.25 per share and 800 common shares at $43.70 per share. 1800 common shares held in the treasury are reserved for exercise of these options. All of these options were exercised in January and February 1959.

Also at January 3, 1959, stock options for 42,060 common shares at prices ranging from $35.75 to $47.98 per share were outstanding under the stock option plan approved by shareholders on March 21, 1957. Each option expires five years after grant but not later than January 1, 1966. 20% of the shares covered by each option becomes exercisable ten months after grant of the option and an additional 20% becomes exercisable each year thereafter. At January 3, 1959, options for 2240 shares were exercisable.

Lease Commitments

At January 3, 1959, the company and its subsidiaries have 771 leases expiring after three years from that date (some of which contain percentage rental clauses) with minimum annual rentals amounting to approximately $12,192,000 exclusive of taxes, insurance and maintenance payable by the lessee. Of this amount, approximately 71% applies to leases expiring within 10 years.

Proposed Changes in Capital Stock

On February 9, 1959, The Board of Directors voted, subject to shareholders approval at the annual meeting on March 23, 1959, to (1) increase the number of authorized common shares from 4,300,000 to 10,000,000 shares (2) reduce the par value from $5.00 to $4.00 per share (3) change each of the presently issued $5.00 par value common shares to three issued shares of $4.00 par value per share and (4) to eliminate the 30,000 shares of authorized but unissued cumulative preference shares.

A new restricted stock option plan also was approved, subject to shareholders authorization, for 100,000 shares of the new $4.00 par value stock for issuance to executives and key employees.

ARTHUR ANDERSEN & CO.

120 South LaSalle Street
Chicago 3

To the Shareholders,
National Tea Co.:

We have examined the consolidated balance sheet of NATIONAL TEA CO. (an Illinois corporation) AND SUBSIDIARIES as of January 3, 1959, and the related statements of consolidated income and surplus for the fifty-three weeks then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We had made a similar examination for the fifty-two weeks ended December 28, 1957.

In our opinion, the accompanying consolidated balance sheet and statements of consolidated income and surplus present fairly the financial position of National Tea Co. and Subsidiaries as of January 3, 1959, and the results of their operations for the fifty-three weeks then ended, and were prepared in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding fifty-two week period.

ARTHUR ANDERSEN & CO.

Chicago, Illinois,
February 13, 1959.

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serving you better . . . saving you more . . .

NATIONAL
FOOD STORES